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Supreme Court of the United States

OCTOBER TERM, 1942.

No. 836

WALTER S. HALLIWELL, *Petitioner,*

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

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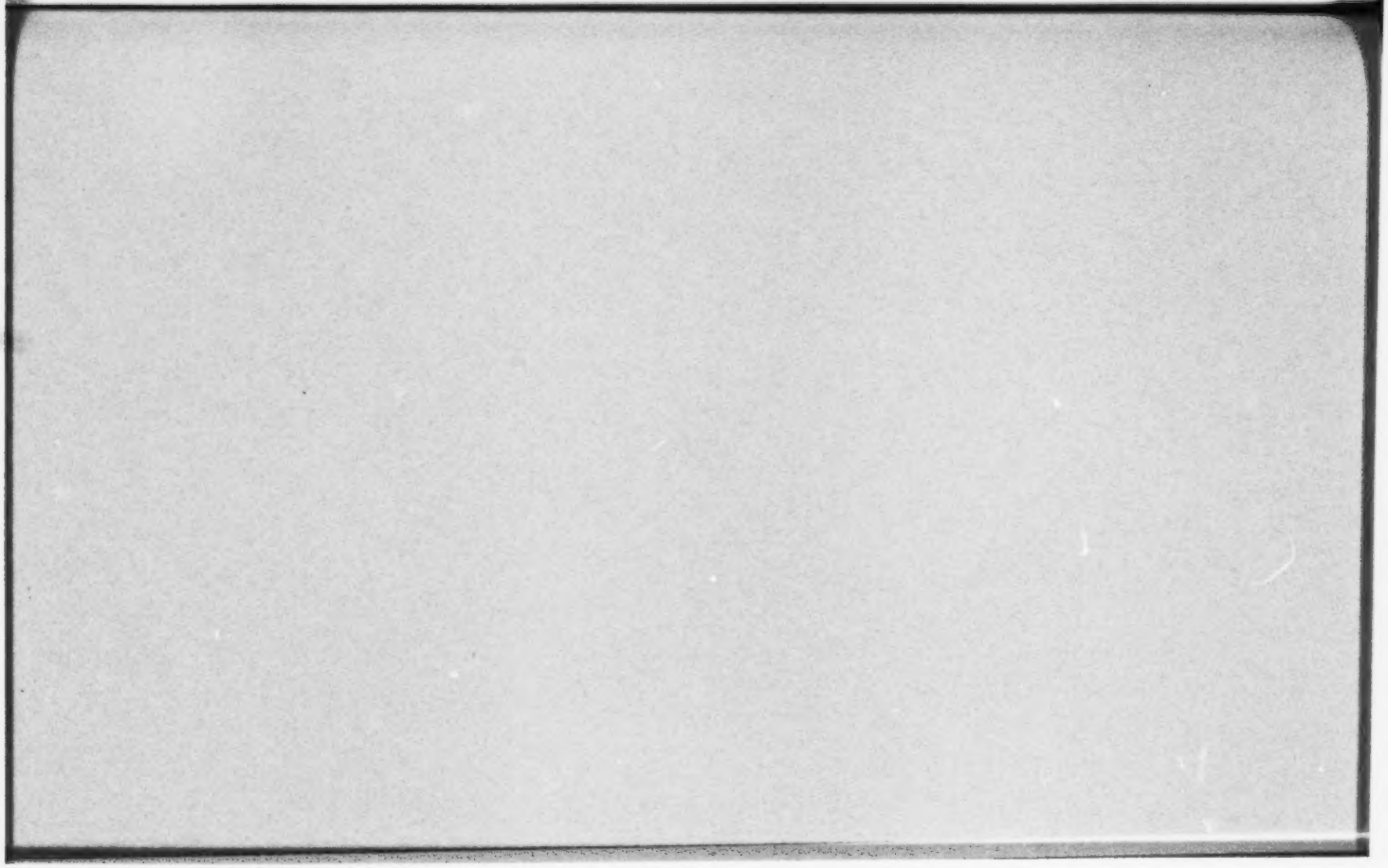

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Supreme Court of the United States

OCTOBER TERM, 1942.

No. .....

WALTER S. HALLIWELL, *Petitioner,*

vs.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

The petitioner, Walter S. Halliwell, prays that a writ of certiorari be issued to review the judgment of the United States Circuit Court of Appeals for the Second Circuit, entered in the above entitled cause December 17, 1942 (R. 49) reversing the decision of the United States Board of Tax Appeals (R. 26).

The certified transcript of the record in this case, including the proceeding in the Circuit Court of Appeals, is furnished herewith in accordance with Rule 38, Paragraph I, of the Rules of this Court.

The Opinions Below.

The decision of the United States Board of Tax Appeals is reported in 44 B. T. A. 740 (R. 26-36). The decision of the court below reversing the Board is reported in 131 F. (2d) 642 (R. 48).

Jurisdiction.

The judgment of the Circuit Court of Appeals for the Second Circuit was entered December 17, 1942 (R. 50). The jurisdiction of this Court is invoked under Section 240 a of the Judicial Code as amended by the Act of February 13, 1925 (43 Stat. 938) and by Sections 1141 and 1142 of the Internal Revenue Code. (53 Stat. 164, 165.)

The Question Presented.

Did the petitioner realize taxable gain, under Sections 111, 112 and 113 of the Revenue Act of 1938 (52 Stat. 485) on the transfer to his wife, in proceedings for divorce, of certain securities specified in and transferred pursuant to the decree of the divorce court?

Summary Statement of Matter Involved.

The petitioner married Lillian de Melinowska May 31, 1920, and on March 3, 1938, she instituted in the Superior Court for Lithfield County, Connecticut, an action for divorce, custody of a minor child of the marriage and for alimony. Following the institution of the suit for divorce and on March 3, 1938, the parties entered into a written agreement which is Exhibit 8 at page 18 of the Record.

Therein they agreed, subject to the approval of the divorce court, that, in the event of a decree of divorce, the petitioner should transfer certain securities "described in Schedule 'A' " to his wife and she should accept the same in satisfaction of any and all claims that she may have by way of alimony and for her support and for the support of their child.

On July 12, 1938, a judgment was entered by the superior court in the action instituted by Lillian against the petitioner. (Exhibit 11, page 23 of R.) The court approved the agreement entered into between the petitioner and Lillian and found, *inter alia,* that the petitioner was possessed of property having an approximate value of $1,500,000 and that securities and cash of the approximate value of $462,561.00 were a reasonable portion of his property to be assigned to her in accordance with the terms of the agreement. The court stated:

> Securities and cash of the approximate value of $462,561.00 are a reasonable portion of the defendant's estate to be assigned to the plaintiff as provided by and in compliance with the terms of the agreement aforesaid.

The court decreed that Lillian was divorced, should have the custody of their minor child and:

> the defendant on or before the 16th day of July, 1938, shall pay over, assign, transfer, and deliver to the plaintiff as alimony and in full of his obligation for the support of said minor child, securities and cash, or substitutes therefor, of the approximate value of $462,561.00, as follows:

Shares		*Amount*
180	American Snuff Co. Com. at 51¼	$ 9,225.00
545	American Tobacco Com. B. at 66¼	36,106.25
2,875	American Tobacco Com. A at 67	192,625.00
4,435	British American Tobacco ordinary Pound shares at 26.	115,310.00
1,591	Imperial Tobacco, ordinary Pound shares at 35⅓	56,281.62

Shares		*Amount*
50	MacAndrews & Forbes Co. Com. at 29¾	1,487.50
92	United States Tobacco Com. at 32	2,944.00
38	Porto Rican American Tobacco Co. Com. A. at 2⅜	90.25
1,288	R. J. Reynolds Tobacco Co. Com. B. at 38½	47,278.00
6	J. S. Young Co. Com. at 90	540.00
		$461,887.62
	Cash	673.38
		$462,561.00

and it is

> Further adjudged, that upon the delivery to the plaintiff of the foregoing securities and cash, the defendant shall be, and he hereby is, discharged of all past or future obligations for the support of the plaintiff, Lillian J. Halliwell, or the minor daughter of the parties, Lillian Ann Halliwell.

On July 16, 1938 the specified securities and the $673.38 cash were delivered and paid to Lillian. The cost of the specified securities to the petitioner was $160,038.97. At the time of their delivery to his divorced wife the value of the securities was $461,887.62.

The Commissioner of Internal Revenue determined that the difference between the cost of the securities and their value at the date of delivery constituted capital gain which should be taken into account in computing the net income of the petitioner for 1938.

The Board of Tax Appeals reversed the Commissioner and held the transaction did not give rise to tax liability. (R. 33, 37.) The United States Circuit Court of Appeals for the Second Circuit in turn reversed the Board and held the transaction gave rise to taxable gain under Sections 111, 112 and 113 of the Revenue Act of 1938 as the result of a sale or exchange of property.

The court stated:

> The gain so realized must be taken into account in determining his income tax. Revenue Act of 1938, §§ 111, 112, 113, 117; 52 Stat. 484.

Specification of Errors To Be Urged.

The court below erred:

1.

In holding the transfer of the securities constituted a "sale" or "exchange of property" for which an "amount" was received and in holding sections 111, 112 and 113 of the Revenue Act of 1938 apply.

2.

In not holding the transfer of the securities pursuant to the divorce decree operated as a division or partition of property based on marital rights and not a "sale or exchange" or "other disposition of property."

3.

In not holding the divorce court ordered merely the assignment of the securities specified "as follows" in Schedule "A" to Lillian and did not render a money judgment giving rise to an obligation to be satisfied by the transfer of the securities.

4.

In not holding the transaction, by which the petitioner transferred property to Lillian pursuant to the divorce de-

cree, was one whereby nothing of exchangeable value came to or was received by him and that the transfer did not give rise to or create taxable income within the meaning of Section 111 (a) of the Revenue Act of 1938.

5.

In not holding the decision in *Commissioner v. Mesta*, 123 F. (2d) 986 (Third Circuit) is not controlling. The cases are distinguishable, as are the marital laws of the states of domicile and the facts presented in the two cases.

Reasons for the Allowance of the Writ.

1.

The court below held that the transfer of certain securities by the petitioner to his wife, which was pursuant to the decree of divorce in the superior court of Connecticut, that the securities were a reasonable portion of his estate to be assigned to her, constituted a "sale or exchange" of the securities within the meaning of Section 112 (a) of the Revenue Act of 1938. In so holding the court below has given the provision of the revenue act an interpretation never before placed on it by Treasury Department Regulations, the Board of Tax Appeals, or the courts. The question presented is of public importance, in that it concerns all divisions or partitions of property in divorce proceedings and in partition agreements and suits as well. The holding is that such transactions amount to sales or exchanges resulting in the realization of gain or loss. The questions has never been passed on by this court, but should be.

2.

The court below reached a conclusion in conflict with the express wording of the Revenue Act which is that there must be a sale or exchange of property and the amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property, other than money, received. See Appendix.

3.

The decision below is in conflict with the applicable Treasury Regulations 101, promulgated under the Revenue Act of 1938, Articles 111-1, 112 (a)-1, 113 (a)-1, 2 and 117 (2).

In Article 111-1, it is provided:

> Except as otherwise provided, the Act regards as income or as loss sustained, the gain or loss realized from the conversion of property into cash, or from the exchange of property for other property differing materially either in kind or in extent. The amount realized from a sale or other disposition of property is the sum of any money received plus the fair market value of any property which is received.

4.

The court below gave no consideration to applicable statute of the state of divorce. Under Section 5156 of the General Statutes of Connecticut the wife is, on the death of her husband, entitled to the use for life of one-third in value of all the property owned by him. The court below reached a conclusion which does not give proper effect to the statute and is in direct conflict with the decisions of the highest

court of Connecticut in *Lyon v. Lyon,* 21 Conn. 185 and *Scott v. Scott,* 83 Conn. 634, in each of which cases the court stated:

> Such a decree and assignment is specific in its character, and operated as a division or partition, between the husband and wife, of his property, in such proportion as the court by its decree determines.

The court below held the transaction a sale or exchange, while the state court has consistently held such a decree operates as a division or partition of his property between them. The divorce court assigned her portion to the divorced wife.

The Board of Tax Appeals gave effect to the decisions of the Connecticut court. The decision of the Court of Appeals is in direct conflict with the numerous decisions of this Court that the local law of a state is as announced by the state court of last resort. *Clarke v. Clarke,* 178 U. S. 186, 20 S. Ct. 873, 44 L. Ed. 1028, aff'g 70 Conn. 483, 40 A. 111.

5.

The holding of the court below that the wife had no present right in the securities owned by the petitioner is in direct conflict with the decision of this court in *Audubon v. Shufeldt,* 181 U. S. 577, 21 S. Ct. 735, 45 L. Ed. 1010, in which this court held alimony arises from the relation of marriage and is regarded as a portion of the husband's estate, to which she is entitled by virtue of marriage. Her right resulted from marriage and by way of instantaneous gift from the state, not by way of gift from the respondent. *Ferry v. Spokane P. & S. R. Co.,* 258 U. S. 314, 42 S. Ct. 358, 66 L. Ed. 635, 20 A. S. R. 1326; *Bowers v.*

Bonert, 184 N. Y. S. 274, 112 Misc. 612; *Kursheedt v. Union Dime Sav. Inst.*, 118 N. Y. 358, 23 N. E. 473, 7 L. R. A. 229. It vested at the marriage in all the property of which he was then seized and in all his property thereafter acquired and in all increments and increases thereto. It vested in each of the securities in Schedule "A" at the time of marriage or at the time acquired. At every moment thereafter Lillian was entitled to her share in any increase or enhancement in value of any of the securities, because they were property "owned" by the respondent and her interest was that to the use of one third "in value" at the time of his death whenever it might occur. Her interest was in the $160,038.97 cost of the securities and in each dollar's advance in value up to the $461,887.62.

6.

The divorce court decreed the transfer of specific securities listed and itemized in the decree and did not render a money judgment that later might have been satisfied by the transfer of property instead of cash. There was no contractual obligation to pay as in *Bowers v. Kerbaugh-Empire Co.*, 271 U. S .170, 46 S. Ct. 449, 70 L. Ed. 886.

7.

The decision of the court below is in direct conflict with the decision of the Seventh Circuit in *Kalman Hirsch v. Commissioner*, 115 F. (2d) 656 and with the decision of the Fifth Circuit in *Dallas Transfer etc. Co. v. Commissioner*, 70 F. (2d) 95, in which Judge Walker stated:

> "Taxable income is not acquired by a transaction which does not result in the taxpayer getting or having anything he did not have before. *Gain or profit* is essential to the existence of taxable income. Commis-

sioner of Internal Revenue v. Rail Joint Co. (C. C. A.) 61 F. (2d) 751, 752, Bowers v. Kerbaugh-Empire Co., 271 U. S. 170, 46 S. Ct. 449, 70 L. Ed. 886; Burnet v. John F. Campbell Co., 60 App. D. C. 197, 50 F. (2d) 487."

8.

The court below erred in following the decision of the Third Circuit in *Commissioner v. Mesta,* 123 F. (2d) 986, which arose under the law of the State of Pennsylvania that alimony can not be decreed when an absolute divorce is granted and in which case Judge Biggs stated that Mesta delivered stock in discharge of "his obligation under contract." The decision below should be found to be in conflict with the reasoning of Judge Biggs in the Mesta case and the emphasis he places on the law of the State of Pennsylvania and the actual facts before him. If not reviewed and reversed by this Court, the court below, by following the Mesta case, will have established a rule and started a line of decisions in direct conflict with and entirely without the expressed intent of the Congress in the several revenue acts.

Conclusion.

Counsel for the petitioner believes that this writ should be granted for the simple reason that the court below gave so little consideration to and departed so far from the clearly stated requirements of the statute, which are, there must be a "sale or exchange" or "other disposition of property" with an "amount realized therefrom" (52 Stat. 485) and from the regulations which are the "conversion of property into cash" or "other property" (Regulations 101, Article 111-1).

If the transaction be looked at as the satisfaction of an obligation for less than its amount, then the writ should be granted because the court below ignored the fact that the wife's right arose at marriage and attached to and rested in all his property then had or thereafter acquired and in all increases thereto, so held in Ferry v. Spokane P & S R. Co., 258 U. S. 314, 42 S. Ct. 358, 66 L. Ed. 635 with which the decision below is in direct conflict.

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APPENDIX.

Revenue Act of 1938, c. 289, 52 Stat. 447:

SEC. 111. DETERMINATION OF AMOUNT OF, AND RECOGNITION OF, GAIN OR LOSS.

(a) *Computation of Gain or Loss.*—The gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 113 (b) for determining gain, and the loss shall be the excess of the adjusted basis provided in such section for determining loss over the amount realized.

(b) *Amount Realized.*—The amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received.

(c) *Recognition of Gain or Loss.*—In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recognized for the purposes of this title, shall be determined under the provisions of section 112.

* * * * *

SEC. 112. RECOGNITION OF GAIN OR LOSS.

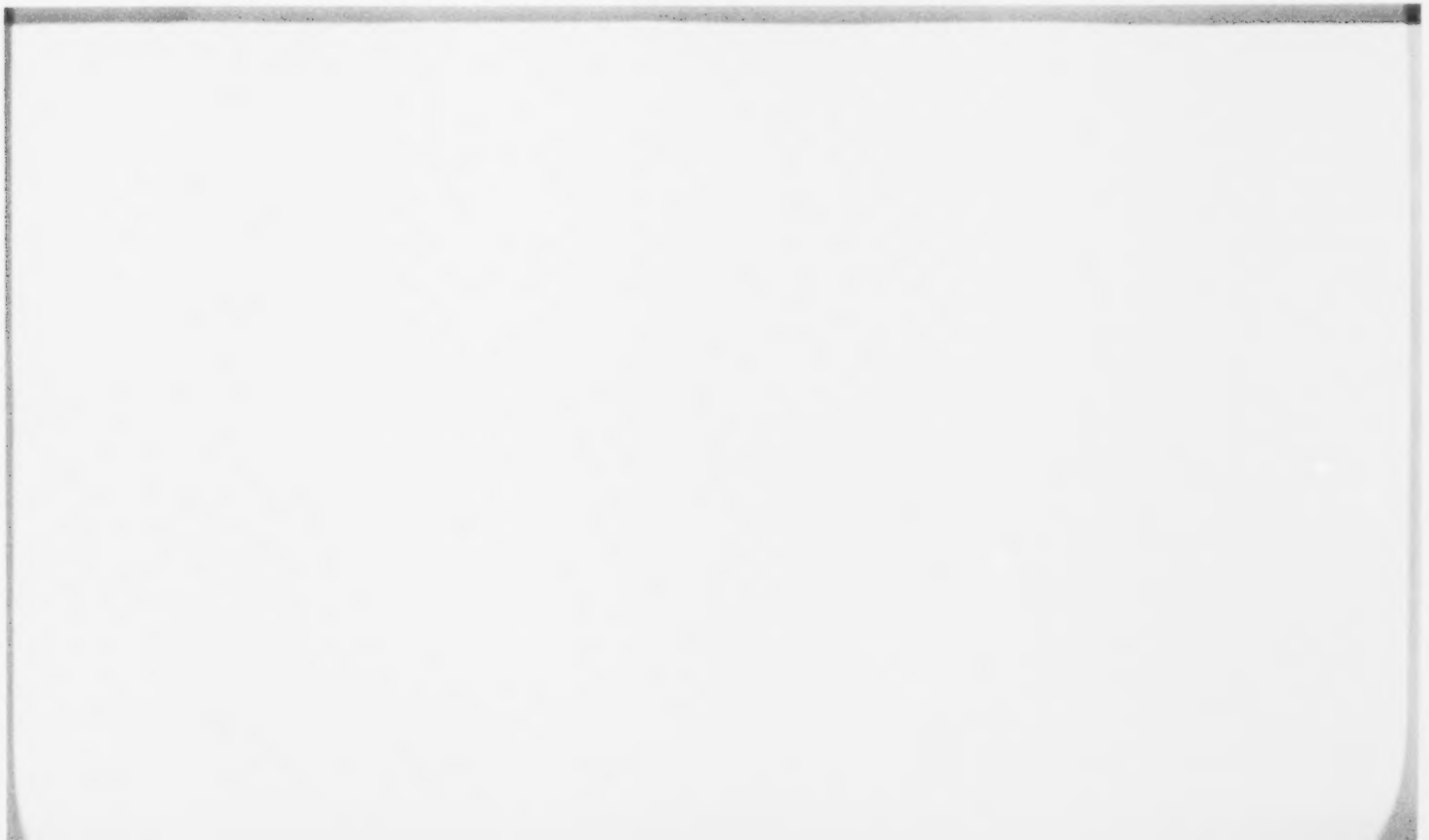
(a) *General Rule.*—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section.

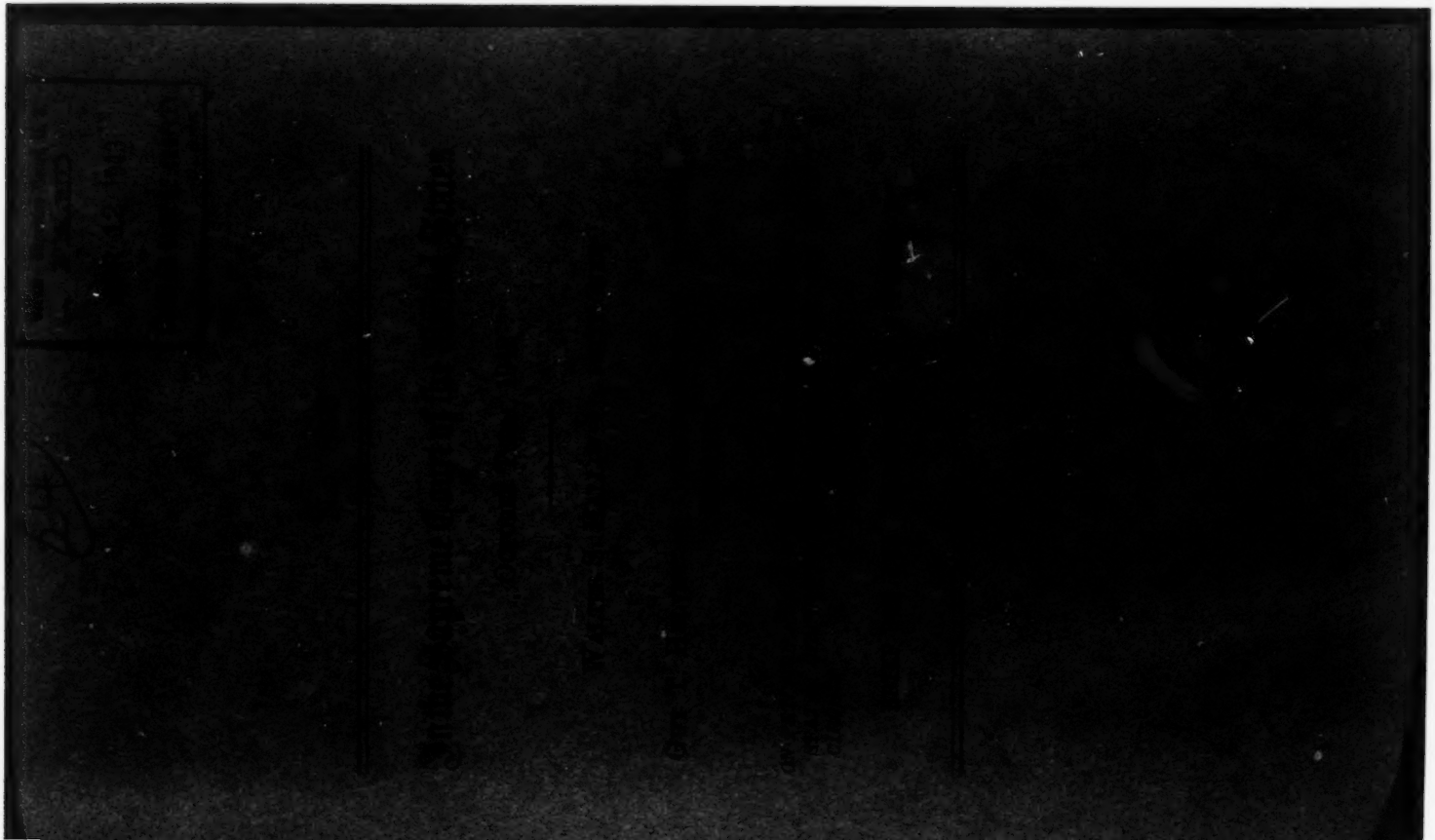
* * * * *

SEC. 113. ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Basis (Unadjusted) of Property.*—The basis of property shall be the cost of such property; except that—

* * * * *





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In the Supreme Court of the United States

OCTOBER TERM, 1942

No. 836

WALTER S. HALLIWELL, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 26–36) is reported in 44 B. T. A. 740. The opinion of the Circuit Court of Appeals (R. 48–50) is reported in 131 F. 2d 642.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered December 17, 1942 (R. 50). The petition for a writ of certiorari was filed March 17, 1943. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

In 1938, pursuant to a divorce decree, the taxpayer transferred to his former wife certain securities which had cost him less than the value at that time of such transfer. Did the taxpayer realize a taxable gain under Sections 111, 112, 113 and 117 of the Revenue Act of 1938?

STATUTE AND REGULATIONS INVOLVED

Revenue Act of 1938, c. 289, 52 Stat. 447:

> SEC. 111. DETERMINATION OF AMOUNT OF, AND RECOGNITION OF, GAIN OR LOSS.
>
> (a) *Computation of Gain or Loss.*—The gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 113 (b) for determining gain, and the loss shall be the excess of the adjusted basis provided in such section for determining loss over the amount realized.
>
> (b) *Amount Realized.*—The amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received.
>
> (c) *Recognition of Gain or Loss.*—In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recognized for the purposes of this title, shall be determined under the provisions of section 112.
>
> * * * * *

SEC. 112. RECOGNITION OF GAIN OR LOSS.

(a) *General Rule.*—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section.

* * * * *

SEC. 113. ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Basis (Unadjusted) of Property.*—The basis of property shall be the cost of such property; except that—

* * * * *

SEC. 117. CAPITAL GAINS AND LOSSES.

* * * * *

(b) *Percentage Taken Into Account.*—In the case of a taxpayer, other than a corporation, only the following percentages of the gain or loss recognized upon the sale or exchange of a capital asset shall be taken into account in computing net income:

100 per centum if the capital asset has been held for not more than 18 months;

66⅔ per centum if the capital asset has been held for more than 18 months but not for more than 24 months;

50 per centum if the capital asset has been held for more than 24 months.

* * * * *

The applicable regulations are Treasury Regulations 101, promulgated under the Revenue Act of 1938, Articles 111–1, 112 (a)–1, 113 (a)–1, 2 and 117–2.

STATEMENT

The following facts were stipulated (R. 16–25) and found by the Board of Tax Appeals (R. 27, 29–30):

Taxpayer, a resident of New York (R. 27) married Lillian de Melinowska on May 31, 1920 (R. 29).

On March 3, 1938, Lillian instituted in the Superior Court of Connecticut an action against taxpayer for divorce, custody of a minor child, and alimony (R. 29).

On March 16, 1938, taxpayer and Lillian entered into a written agreement that if a decree of divorce were granted, Lillian, subject to the approval of the court, was to be awarded the custody of their minor child and also a lump sum, consisting of certain securities and cash specified in a schedule attached to the agreement, as alimony, for her support and maintenance, and for the support, maintenance, and education of their minor child. The parties also agreed that, if taxpayer died pending the action for divorce, the securities and cash specified in the schedule attached to the agreement were to be delivered to Lillian in lieu of any and all statutory and other rights in and to taxpayer's estate. In the schedule attached to the agreement the following securities and cash were specified (R. 29):

Security	Shares	Amount
American Snuff Co. com. at 51¼	180	$9,225.00
American Tobacco com. B at 66¼	545	36,106.25
American Tobacco com. A at 67	2,875	192,625.00
British American Tobacco ordinary pound shares at 26	4,435	115,310.00
Imperial Tobacco ordinary pound shares at 35⅜	1,591	56,281.62
MacAndrews & Forbes Co. com. at 29¾	50	1,487.50
United States Tobacco com. at 32	92	2,944.00
Porto Rican American Tobacco Co. com. A at 2⅜	38	90.25
R. J. Reynolds Tobacco Co. com. B at 38½	1,228	47,278.00
J. S. Young Co. com. at 90	6	540.00
		461,887.62
Cash adjustment		673.38
Total		462,561.00

On March 16, 1938, Lillian executed a release in which she released taxpayer, his executors, administrators, and estate from all of her rights to share in his property at his death (R. 29).

On July 12, 1938, a judgment was entered by the superior court in the divorce action. The court approved the agreement entered into between taxpayer and Lillian and found, *inter alia,* that taxpayer was possessed of property having an approximate value of $1,500,000 and that securities and cash of the approximate value of $462,561 were a reasonable portion of taxpayer's property to be assigned to Lillian in accordance with the terms of the agreement. The court ordered that Lillian was divorced from taxpayer; that she was to have the custody of their minor child; and that on or before July 16, 1938, taxpayer was to transfer to Lillian as alimony, and in full satisfaction of his

obligation for the support of their minor child, the securities and cash, or substitutes therefor, of the approximate value of $462,561, specified in the schedule attached to the agreement. The court further ordered that upon delivery of the specified securities and cash taxpayer was to be discharged of all obligations for the support of Lillian or for the support of their minor child. On or about July 16, 1938, the specified securities and cash were delivered to Lillian. The cost of the specified securities to taxpayer was $160,038.97. At the time of their delivery to Lillian the value of the specified securities was $461,887.62. (R. 29–30.)

The Commissioner determined that $301,848.65, being the difference between the cost of the securities and their value at date of delivery to Lillian, constituted capital gain of which 50 per cent should be taken into account in computing the net income of the taxpayer for 1938 (R. 12). The Board of Tax Appeals held this erroneous (R. 33–36) but the court below reversed (R. 48–50).

ARGUMENT

In holding that the taxpayer realized taxable gain on the transfer of securities, pursuant to a decree of divorce, to his former wife, the court below followed the case of *Commissioner* v. *Mesta,* 123 F. 2d 986, where the Third Circuit reached the same conclusion upon substantially similar

facts. This Court denied the application for certiorari in that case, 316 U. S. 695, and we submit that the instant petition should be denied for the same reasons as set forth in our brief in opposition in that case. Since that brief was filed (May 25, 1942), no conflict has developed and certainly there is no conflict with any of the authorities cited by the taxpayer in the petition for certiorari. The regulation to which he refers (Pet. 7)[1] is largely a repetition of the statutory language (Sec. 111 (a) and (b) of the Revenue Act of 1938, *supra*) and plainly is not inconsistent with the instant decision. As pointed out by the court below (R. 49) the cases of *Lyon* v. *Lyon,* 21 Conn. 185, and *Scott* v. *Scott,* 83 Conn. 634, relied upon by the taxpayer (Pet. 7–8) do not support the contention accepted by the Board of Tax Appeals (R. 34–35) that the instant transaction amounted to a mere division of property between husband and wife which would not result in any gain or loss. The securities in question were

[1] Treasury Regulations 101, promulgated under the Revenue Act of 1938:

ART. 111–1. *Computation of gain or loss.*—Except as otherwise provided, the Act regards as income or as loss sustained, the gain or loss realized from the conversion of property into cash, or from the exchange of property for other property differing materially either in kind or in extent. The amount realized from a sale or other disposition of property is the sum of any money received plus the fair market value of any property which is received. * * *

* * * * *

Halliwell's own individual property and prior to the assignment he could have sold them or given them away without her consent. *Newman* v. *Dore,* 275 N. Y. 371, 376–377; *Krause* v. *Krause,* 285 N. Y. 27, 31; see also opinion of the court below and authorities there cited. (R. 49.) In the circumstances the transaction was sufficient analogous to a sale to justify treating it as such for income tax purposes. Cf. *Kenan* v. *Commissioner,* 114 F. 2d 217 (C. C. A. 2d); *International Freighting Corp.* v. *Commissioner* (C. C. A. 2d), decided March 6, 1943 (C. C. H., par. 9334); *Rogers* v. *Commissioner,* 103 F. 2d 790 (C. C. A. 9th), certiorari denied, 308 U. S. 580. Cases such as *Hirsch* v. *Commissioner,* 115 F. 2d 656 (C. C. A. 7th), and *Dallas T. & T. Warehouse Co.* v. *Commissioner,* 70 F. 2d 95 (C. C. A. 5th), cited by taxpayer (Pet. 9) (cf. also *Helvering* v. *American Dental Co.,* decided March 1, 1943, No. 303, present term), stand for the proposition that where a creditor forgives a debt, the debtor does not necessarily realize income in the amount forgiven; but certainly they do not hold that where, as here, an obligation is paid in full by the transfer of securities, the obligor can not realize taxable gain measured by the difference between the cost of the securities and the amount of the obligation or their value at time of transfer.

CONCLUSION

The decision is plainly correct; there is no conflict; the petition should be denied.

Respectfully submitted.

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